

AGENCY COUNSEL BROWN BAG LUNCH – THURSDAY JUNE 13, 2002

RECOMMENDATIONS FOR TERMINATING OR AMENDING CONTRACTS

(1) ESTABLISH COMMUNICATION WITH APPROPRIATE STAFF.

- (a) Make proactive efforts to routinely communicate with fiscal, contract and program staff. CTR Internal Control Guidelines recommend the participation of both the Legal Staff and the Chief Fiscal Officer as the key staff responsible for ensuring fiscal responsibility. Internal department policies should encourage legal staff consultation prior to implementing any action to terminate, reduce or amend a contract, especial during time of fiscal constraints. Program and fiscal staff may not understand the limitations or implications of certain terminations, reductions, suspensions or amendments and legal staff should be included in discussions when these actions are anticipated.
- (b) The Attorney General's Office should also be consulted regarding any anticipated termination, reduction, suspension or amendment which may involve a potential threat of litigation, or which is foreseen to involve a current or potential dispute or difficulty.
- (c) The Office of the Comptroller should be contacted whenever it is anticipated that a Department may be faced with insufficient funds for contract, payroll or other fiscal obligations.

(2) REVIEW POLICIES IN PROCUREMENT HANDBOOK. Staff should review Chapter 5 of "Commonwealth Procurement and Procedures Handbook", which identifies advice and other information regarding termination, amendments and disputes.

(3) CAREFULLY CONSIDER THE "REASONS" FOR TERMINATIONS OR AMENDMENTS. If a termination is "for cause", the department must be able to document the "for cause" events or actions supporting this type of termination, that the performance requirements were clearly outlined in the contract and that the Contractor was, or will be provided with an opportunity to cure. Without cause terminations should provide a reasonable notice of termination for the type of performance sought, or as specified in the contract. Terminations, reductions or amendments for elimination or reduction of appropriation or allotments should be carefully reviewed in relation to the Department's published mission, priorities other legal obligations and available funding.

(4) CAREFULLY REVIEW TERMINATION, SUSPENSION OR AMENDMENT TERMS.

- (a) Termination, suspension and amendment language is contained in the Contract, which includes the contract boilerplate, language in the procurement document (Request for Response –RFR), and additional negotiated terms and conditions.
- (b) A Department's ability to amend, reduce, suspend or terminate a contract or modify contract performance is determined by the terms contained in the contract, the type of performance required, governing statutes and appropriation language. State and federal mandates to provide health and safety services to citizens, services to clients in residence, etc. may also limit a Department's ability to terminate or reduce certain contracts. Other

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contracts have performance, which is not capable of being reduced or divided, which may also limit a Department's ability to reduce or terminate a contract.

- (c) It is recommended that contracts contain language informing Contractors that the contract creates no entitlement or guaranteed funding and is subject to completion and acceptance of performance by the Department. In addition, contract performance requirements are subject to the Department's needs, which are based upon mandates, funding appropriation and allotments, which may change with changes in law, or budget and allotment reductions.
- (d) In the event the Department is faced with a budget reduction, elimination or substantial change in circumstances warranting a change in contract need or performance, the Department should make best efforts to negotiate an amendment to reduce performance, prior to having to terminate or suspend a contract. However, in some cases of severe budget cuts, allotment reductions, or agency funding eliminations, a Department will have no choice but to terminate, reduce or suspend existing contracts. To provide further protection, any contract which has performance which can be broken into phases, or is divisible and capable of being reduced should include language allowing the Department to require a reduction in performance and corresponding maximum obligation in the event of a budget or allotment reduction.

(5) CONSIDER THE "COSTS" OF TERMINATION, AMENDMENTS OR REDUCTIONS.

- (a) Unless otherwise specified in the Contract, the Department is responsible for compensating for reasonable performance requested, received and accepted until the termination or amendment date.
- (b) Departments may not request or accept performance or otherwise incur obligations in excess of Department appropriations and allotments. (M.G.L. c. 29, §26 and §27).
- (c) Certain contracts can be easily terminated without additional costs, since the Department is purchasing services or commodities on an "as needed" basis. Other contracts may require compensation or liquidated damages for the Contractor for an early termination or reduction. Such contracts include those with an anticipated long term commitment, or which require the Contractor to make an up front commitment of time or funding, or to incur additional obligations in order to complete performance, such as renting space, hiring personnel, purchasing equipment or materials. Therefore, the Department needs to factor in these obligations when considering the associated "costs" of termination for the Contractor and the Commonwealth.
- (d) Some contracts may not be terminated without severe penalties. For example, leases and TELPs (Tax exempt lease purchases) have severe penalties for early termination. Lessors and TELP financiers build the cost of the lease or TELP financing to compensate the Contractor over a period of time for the value of the use of equipment, space or financing

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which has been provided to the Commonwealth. In some cases, the penalties equal or exceed the amount due for the entire TELP or Lease period. TELPs can not be terminated without prior approval since failure to repay financing already provided could potentially affect the Commonwealth's bond rating. Usually the only situation allowing the termination of a TELP is total elimination or lack of appropriation or allotment, not just a funding cut, and the Commonwealth would usually seek additional appropriations to repay this financing obligation.

(6) NOTICE OF TERMINATION, AMENDMENT, SUSPENSION OR REDUCTION.

- (a) Notices are usually in the form of a letter distributed to the Contractor(s). Notice of termination must be reasonable (usually not less than 30 days for without cause terminations depending upon the complexity of the contract) in accordance with any notice provisions agreed to as part of the contract (e.g., Human Service Contracts require a longer notice period).
- (b) The content of the notice is usually prescribed in the Contract. For example, in the Commonwealth Terms and Conditions the following language appears. *“Any written notice of termination or suspension delivered to the Contractor shall state the effective date and period of the notice, the reasons for the termination or suspension, if applicable, any alleged breach or failure to perform, a reasonable period to cure any alleged breach or failure to perform, if applicable, and any instructions or restrictions concerning allowable activities, costs or expenditures by the Contractor during the notice period.”*
- (c) For all notices, Department must document a Contractor's actual receipt of notice. (See notice receipt requirements in Commonwealth Terms and Conditions and Handbook, and Standard Contract Form Instructions.
- (d) For Contracts using the new Standard Contract Form and Instructions, the “Contract Manager” is the person to receive notices unless otherwise specified in the Contract. *“Unless otherwise specified in the Contract, legal notice sent or received by the Contractor's Contract Manager (with confirmation of actual receipt) through the listed fax number(s) or electronic mail address will meet any requirements for written notice under the Contract”.* For other types of Contracts (construction, leases, etc.) Departments should carefully review the language for the person and form of receipt of notice which is required.

(7) PROCESS FOR DOCUMENTING AMENDMENTS.

- (a) Contract amendments are made using the Standard Contract Amendment Form (or other appropriate amendment form for construction, leases, etc.), attaching the details of the amendment (date change, change in scope, costs, etc.). The Amendment is sent to the Contractor for signature and must be executed by both parties contemporaneously with the need for the Amendment but in no event later than the termination date in the Contract.

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- (b) In the majority of cases, amendments are mutually agreed to by the parties. Amendments requesting increased performance (as authorized by the procurement or contract) are fairly routine and do not meet resistance by Contractors unless a Contractor is unable (or unwilling) to increase the requested additional performance.
 - (c) However, when faced with budget or allotments cuts, Departments may be faced with situations in which a Contractor refuses to agree to a contract amendment reducing the contract performance and maximum obligation of a contract. In these circumstances special attention must be paid to ensure that the amendments are timely negotiated to prevent obligations in excess of appropriations and allotments, or in the alternative, to provide timely notice of contract termination or suspension, and in all cases to prevent litigation.
 - (d) Departments are also required to reflect any amendment having a fiscal impact (increase, decrease, change in funding source, change in performance dates, rates etc.) in the state accounting system (MMARS) using the appropriate transaction modification form.
- (8) **DEPARTMENT'S ACTIONS MUST BE FAIR AND DEMONSTRATE GOOD FAITH AND FAIR DEALING.**